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Supreme Court, U.S.
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No. 03-1688

In The
Supreme Court of the United States

PT PERTAMINA (PERSERO), f/k/a PERUSAHAAN PERTAMBANGAN MINYAK DAN GAS BUMI NEGARA,

Petitioner,

v.

KARAHA BODAS COMPANY, L.L.C.,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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STATEMENT PURSUANT TO RULE 29.6

Respondent, Karaha Bodas Company, L.L.C., has no parent corporation and no publicly held company owns 10% or more of its stock.

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STATUTES AND RULES

The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 3, implemented by 9 U.S.C. §§ 201 *et seq.* 2, 13, 26, 27

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INTRODUCTION

This is a straightforward commercial case involving the breach by Petitioner PT Pertamina (Persero), f/k/a Perusahaan Pertambangan Minyak Dan Gas Bumi Negara ("Pertamina") of two contracts granting Respondent Karaha Bodas Company, L.L.C. ("KBC") the right to produce and sell electricity generated from geothermal resources in the Karaha Area of West Java, Indonesia (the "Project"). In December 2000, a unanimous three-member international arbitral tribunal held that Pertamina had breached those contracts and ordered Pertamina to pay KBC $261.1 million (the "Award"). As part of its continuing efforts to avoid and delay the enforcement of the Award, Pertamina now claims that this Court should review the unique circumstances in which the arbitrators were appointed and the lower courts' approval of that procedure. For several reasons, this issue does not warrant the Court's review.

First, the decision below does not conflict with the decision of any other court of appeals. Pertamina contends that the Fifth Circuit's decision creates a conflict between that court and four other courts of appeals on the issue of whether a court may defer to arbitrators' decisions regarding the appropriateness of their own appointment. A plain reading of the opinion below, however, demonstrates that the Fifth Circuit (and the district court for that matter) did not defer to the arbitrators on this issue. Instead, the Fifth Circuit conducted its own review of the facts and parties' agreements before holding that the arbitrators were properly appointed. The decision below thus does not conflict with the decision of any other court of appeals.

Second, even if the Fifth Circuit had deferred to the arbitrators on this issue, this case still would not present a circuit conflict that this Court should resolve. Each of the four cases on which Pertamina relies in claiming that a circuit conflict exists was decided before this Court's recent opinion in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003), which held that courts must defer to arbitrators on matters of arbitration procedures and scope unless they are so-called "gateway matters." *Id.* at 452. In the year since *Green Tree Financial* was decided, no court has considered whether the propriety of an arbitrator's appointment is a "gateway matter" that calls for *de novo* judicial review. Thus, no conflict exists among the circuits on this issue.

In addition, each of the four appellate decisions cited by Petitioner involved a domestic arbitration, governed by the Federal Arbitration Act, 9 U.S.C. §§ 1-16. This case, by contrast, is an international arbitration, governed by the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention") (incorporated into United States law and codified at 9 U.S.C. §§ 201-208). Unlike the Federal Arbitration Act, the New York Convention has a specific provision addressing whether the confirmation and enforcement of an international award should be rejected because of the manner in which arbitrators are appointed. *See* 9 U.S.C. § 201, Art. V(1)(d) (recognition and enforcement of an award may be refused only if a party establishes that the "composition of the arbitral authority . . . was not in accordance with the agreement of the parties"). That provision was not at issue in any of the cases on which Pertamina relies, and for this separate reason, no conflict is presented here.

Third, even if a circuit conflict arguably existed regarding whether a court may defer to arbitrators' decisions

concerning the appropriateness of their own appointment, this would not be an appropriate case in which to address such a conflict. The decision below is supported by several alternative holdings, including: (1) Pertamina waived its right to object to the manner in which the arbitrators were appointed; and (2) Pertamina failed to prove that it suffered any prejudice as a result of the alleged improper appointment. Moreover, although Pertamina challenges the validity of the arbitrators' appointment under only one of the two contracts between Pertamina and KBC, the Award held Pertamina liable under *both* contracts. As a result, even if Pertamina prevailed on its challenge to the arbitrators' appointment under the first contract, it would remain liable to KBC under the second contract, where the validity of the arbitrators' appointment is not contested. For these reasons, a decision in Pertamina's favor on the question presented would not affect the outcome of this case.

This petition represents nothing more than Pertamina's most recent effort to thwart the international arbitration process to which it agreed when it entered into its contracts with KBC. The Award, issued almost four years ago by a unanimous and prestigious international tribunal, Pet. App. 58a-61a, remains unsatisfied. In addition to its repeated appeals, Pertamina has resolutely refused to post an appellate bond and has vigorously fought all efforts by KBC to collect the Award. Indeed, in a prior opinion arising from this same arbitration, the Fifth Circuit characterized Pertamina's efforts as "certainly sufficient grounds to find Pertamina's behavior dubious and somewhat deceptive." *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi*

Negara, 335 F.3d 357, 369, n.50 (5th Cir. 2003).[1] Pertamina's continued attempts to avoid its contractual obligations have threatened the integrity of international arbitration as a speedy and efficient dispute resolution mechanism and should be rejected.

COUNTER-STATEMENT OF THE CASE

In affirming the district court's decision confirming the Award, the United States Court of Appeals for the Fifth Circuit explained that "the length of this opinion reflects the number of arguments Pertamina raises to evade its obligations under the Award more than the strength of those arguments." Pet. App. 3a. Pertamina now relies on only one of those arguments, but in so doing misrepresents and omits significant facts from the voluminous record. KBC thus submits this counter-statement of facts.

The Parties, The Contracts, And The Project. Petitioner Pertamina is an oil, gas, and geothermal energy company wholly owned by the Government of the Republic of Indonesia. Pet. App. 4a. Respondent KBC is a geothermal energy exploration and development company that builds electric generating stations; its principal investors include Florida Power & Light Company. *Id.*; Pet. App. 7a. Pursuant to two contracts executed in 1994, KBC was granted the right to develop, produce, and sell at contractually guaranteed

[1] *See also id.* at 372, n.60 (finding Pertamina to be "acting in bad faith by pursuing the annulment in Indonesia"); *id.* at 373 ("It is true that Pertamina is likely in the wrong here."); *id.* at 375 ("We empathize with the district court and share its frustrations at the acts of Pertamina and its counsel.").

prices electricity generated from geothermal sources in the Project area. *See* Pet. App. 4a, 57a.

The first contract, the Joint Operation Contract ("JOC") between KBC and Pertamina, granted KBC the right to develop resources in the Project area sufficient to supply a power plant of up to 400 megawatts of generating capacity; to deliver the electricity to Pertamina; and to receive payment from the state-owned electric utility, PT (PLN) Persero ("PLN"), for that electricity. *See* Pet. App. 4a, 57a. The second contract, the Energy Sales Contract ("ESC") among KBC, Pertamina, and PLN, in turn obligated PLN to purchase all of the electricity generated by KBC at guaranteed U.S. dollar-denominated prices. *See* Pet. App. 241a.

The contracts had virtually identical arbitration provisions. Both contracts required the parties to arbitrate any disputes in Geneva, Switzerland, pursuant to the Arbitral Rules of the United Nations Commission on International Trade Law (the "UNCITRAL Rules"). Pet. App. 4a, n.7. Both contracts required the parties to appoint arbitrators in the first instance: the JOC provided that "[e]ach party will appoint an arbitrator," and the ESC provided that "PLN on one hand, and [KBC] and PERTAMINA on the other hand, will each appoint one arbitrator." *Id.* Both contracts also provided that the two appointed arbitrators would "jointly appoint a third arbitrator within thirty (30) days of the date of the appointment of the second arbitrator, to act as Chairman of the Tribunal." *Id.* And both contracts granted the Secretary General of the International Center for Settlement of Investment Disputes ("ICSID") the authority to appoint an arbitrator in the event that an arbitration was commenced but a party failed to appoint an arbitrator within thirty days. *Id.*

The JOC and ESC were expressly incorporated into one another. The JOC provided that the ESC "shall be an integral part of this contract, and to the extent that provisions of the [ESC] obligate the parties hereto, shall be deemed incorporated into this contract for all purposes," while the ESC provided that it and the JOC constituted the entire agreement among the parties. Pet. App. 27a, n.58.

From 1994 through 1997, KBC fully performed its obligations under both agreements, investing approximately $93.1 million to explore, develop, and construct fields for the Project. Pet. App. 245a. By December 1997, KBC had drilled wells and developed geothermal fields in the Project area containing at least 210 megawatts of exploitable geothermal capacity. Pet. App. 204a.

The Dispute And Nomination Of Arbitrators. By Presidential Decree dated January 10, 1998, the Government of Indonesia indefinitely suspended the Project. Pet. App. 6a. Three and one-half months later, on April 30, 1998, KBC initiated arbitration against Pertamina, PLN, and the Government of Indonesia (together, the "Arbitration Respondents") claiming that the cancellation of the Project constituted a breach of both Project contracts. *Id.*; Pet. App. 218a. KBC's claim was based substantially on the fact that both contracts allocated to Pertamina and PLN the risk of a contractual default caused by a "Government Related Event," such as the Government's suspension of the Project. Pet. App. 218a, 8a.

In its notice of arbitration, KBC appointed Professor Piero Bernardini, vice-chair of the International Chamber of Commerce's International Court of Arbitration ("ICC") and member of the London Court of International Arbitration, to serve as an arbitrator. Pet. App. 6a. KBC served its

notice of arbitration on each of the Arbitration Respondents. Pet. App. 160a.

After the thirty-day period had elapsed without the appointment of an arbitrator by Pertamina or any other Arbitration Respondent – and without any communication whatsoever from any Arbitration Respondent regarding the notice of arbitration – KBC notified ICSID that Pertamina and the other Arbitration Respondents had failed to nominate an arbitrator. Pet. App. 30a-31a. That June 2, 1998 letter, as well as ICSID's letter confirming that it was received, was served on each Arbitration Respondent. Pet. App. 59a. Thereafter, KBC responded to questions from ICSID's legal adviser concerning the consolidation of disputes under the two contracts and the appointment of an arbitrator by KBC; that letter was again served on each Arbitration Respondent. Pet. App. 31a, 160a. On June 23, 1998, ICSID sent all of the foregoing correspondence to each Arbitration Respondent by fax and courier. Pet. App. 160a.

In a letter to all parties dated June 29, 1998, ICSID recounted the foregoing correspondence, noted the Arbitration Respondents' failure to respond, and requested the parties' comments by July 13, 1998, on the appointment of Dr. Ahmed El-Kosheri, another vice-chair of the ICC, as the second arbitrator. Pet. App. 31a. On July 1, 1998, KBC responded that it had no objection to such an appointment; that letter was also served on each Arbitration Respondent. Pet. App. 59a, n.4; 160a. The next day, ICSID confirmed receipt of KBC's letter, again copying the Arbitration Respondents. Pet. App. 59a, n.4. On July 10, 1998, ICSID again forwarded the foregoing correspondence to each Arbitration Respondent. *Id.*

On July 13, 1998, ICSID notified the Arbitration Respondents that it intended to appoint Dr. El-Kosheri as a member of the three-person tribunal. Pet. App. 31a. Pertamina and the other Arbitration Respondents again failed to respond, and on July 15, 1998, ICSID appointed Dr. El-Kosheri, who accepted the nomination. *Id.* On July 23, 1998, the two appointed arbitrators selected Mr. Yves Derains, former Secretary General of the ICC, as presiding arbitrator, and notified the parties of that nomination. *Id.*; Pet. App. 161a.

Pertamina has never argued in these confirmation proceedings that it failed to receive KBC's April 30, 1998 notice of arbitration or any of the letters regarding the appointment of the arbitrators.[2] Nonetheless, at no time during the two and one-half months following KBC's notice of arbitration did Pertamina respond to any of this correspondence, let alone raise any objection to the appointments of Professor Bernardini or Dr. El-Kosheri, or to their selection of Mr. Derains.[3] Pet. App. 31a, 59a-60a.

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[2] Pertamina attempts to attribute its initial failure to object to the appointment process to the alleged statements by a KBC employee in Indonesia, Robert McCutchen. *See* Pet. 9. Pertamina never raised this argument in the arbitration during its preliminary challenge to the manner in which the arbitrators were appointed, although it did attempt to rely on those statements during the later merits phase as an excuse for its breaches of contract. The tribunal rejected this argument as having "no relevance." Pet. App. 226a. Although Pertamina argued during the preliminary arbitration proceedings that it failed to name an arbitrator because it did not receive certain correspondence and because it had decided to contest the legitimacy of the arbitration itself, it did not make these arguments in the district court. *See* Pet. App. 33a, n.63; 72a, n.11.

[3] In fact, as noted by the district court, "Pertamina expressly informed the Tribunal [during the preliminary proceedings] . . . that it had no objection to Dr. El-Kosheri, the arbitrator appointed by the

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Pertamina omits from its petition any discussion of these extensive attempts by KBC and ICSID to notify Pertamina of the appointment proceedings and to seek its comments. Instead, Pertamina remarkably claims that the arbitrators were appointed "over Pertamina's timely and strenuous objection." Pet. 4.

The Preliminary Award Proceedings. Prior to the first procedural meeting in the arbitration, Pertamina and the other Arbitration Respondents, all represented by the same lawyers, finally appeared to request that the arbitrators consider certain preliminary procedural issues. In particular, they argued *inter alia* that the Government of Indonesia was not a proper party; that KBC's claims under the JOC and the ESC could not be consolidated into a single arbitration; and that the method by which the arbitrators were appointed violated the ESC. *See* Pet. App. 60a, 168a.

Following the submission of evidence, briefing and a hearing, the arbitrators agreed with the Arbitration Respondents that the Government of Indonesia was not a proper party,[4] but rejected each of the Arbitration Respondents' other preliminary challenges. *Id.*

With respect to the arbitrators' appointment, the tribunal held that the parties could not have intended that KBC and Pertamina jointly appoint a single arbitrator to adjudicate a dispute between them, Pet. App. at 194a-195a,

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ICSID. Thus, Pertamina's objection is solely to the fact that KBC was allowed to select one of the arbitrators." Pet. App. 72a, n.12 (citation omitted).

[4] Although the Government of Indonesia was dismissed as a party to the arbitration, it relies on its ownership of Pertamina as the basis for thereafter continuing to appear as an *amicus curiae* in this and related cases.

noting that this "would defy common sense." Pet. App. 195a. Instead, the arbitrators concluded that the parties did not expressly provide for such a situation, and left the appointment of arbitrators in such circumstances to be conducted under the UNCITRAL Rules, which authorized the appointment procedures used here.[5] Pet. App. at 194a-195a. The arbitrators also observed that the Arbitration Respondents had never claimed that they were declining to respond to the notice of arbitration because jointly nominating an arbitrator would violate the ESC, Pet. App. 196a, and that the decision did not create any unequal treatment for Pertamina because all three members of the tribunal were neutral arbitrators. Pet. App. 196a-197a.

Proceedings On The Merits. Over the next nine months, the remaining parties – KBC on the one hand, and Pertamina and PLN on the other – submitted documentary evidence, written witness statements, expert reports and substantial briefs on the merits of the dispute. *See* Pet. App. 208a-214a. During the five-day trial, which began on June 19, 2000, and ended on June 23, 2000, the tribunal heard live testimony from seven witnesses, as well as extensive argument by counsel on various liability and damages issues.[6] Pet. App. 214a. The parties submitted post-hearing briefs on August 7, 2000. Pet. App. 215a.

On December 18, 2000, the tribunal issued the Award, holding that Pertamina had breached the JOC and the

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[5] Pertamina has never contended that the appointment of the arbitrators was inconsistent with the UNCITRAL Rules.

[6] Both sides declined to cross-examine witnesses who had submitted written statements; notably, Pertamina and PLN declined to cross-examine KBC's damages expert, a professor at the Harvard Business School. *See* Pet. App. 247a, 214a.

ESC and that PLN had breached the ESC. Pet. App. 262a. The tribunal found that both contracts allocated to Pertamina and PLN the risk of a contractual loss caused by a "Government Related Event" such as the suspension of the Project by the Presidential Decree: the contracts placed "the consequences of a Governmental decision which prevents the performance of the contract at PERTAMINA's and PLN's sole risk." Pet. App. 225a. The tribunal awarded KBC $111.1 million – the amount KBC had actually expended on the Project plus interest – as well as $150 million in lost profits, explaining in detail how it arrived at that lost-profits award and the reasons it had rejected the substantially larger amount ($512.5 million) that KBC sought. Pet. App. 239a-247a, 253a-259a.[7]

Pertamina also suggests that lost profits should not have been awarded because the Project had made no progress, but the tribunal expressly rejected this argument in finding that KBC's investment of $93.1 million on

[7] Although it no longer challenges the award of lost profits, as it did unsuccessfully below, Pertamina implies that there was no evidentiary support for that decision. To the contrary, KBC presented substantial evidence supporting its lost-profits claim, including numerous fact witnesses, an expert on geothermal exploration and development, and a damages expert. *See* Pet. App. 247a-249a, 253a-259a. Pertamina also asserts that lost profits were awarded based on a Project "for which no financing was ever committed," Pet. 25, but neglects to mention that the arbitrators expressly rejected this contention, finding that: "[r]egarding the financing necessary for the Project development, there is no reason in the Arbitral Tribunal's opinion to cast doubts about the Claimant's readiness, directly and/or through its shareholders to make provision thereof." Pet. App. 257a. As the Fifth Circuit explained, "the Tribunal appears to have given all of the evidence as to damages, including the availability of financing, appropriate weight in determining liability and damages . . . testimony about FPL's willingness to provide financing was only one factor relevant to damages." Pet. App. 40a.

the Project were "proven and uncontested expenditures." Pet. App. 245a. With respect to the available capacity on which KBC's lost-profits claim was based, the tribunal found that the Arbitration Respondents' arguments "appear[ed] unjustified" – although the tribunal did calculate KBC's lost profits based on a smaller projection of available capacity. Pet. App. 257a.

In reaching its decision, the tribunal cited two other arbitral awards regarding power projects indefinitely suspended by the January 10, 1998, Presidential Decree. Pet. App. 243a, 253a. In both of those cases (the "*Himpurna*" and "*Patuha Power*" cases) an international arbitral tribunal unanimously held that PLN had breached an Energy Sales Contract identical in all relevant respects to the ESC among KBC, Pertamina and PLN, and awarded the claimants $391,711,652 and $180,570,322, respectively.[8] *See* Pet. App. 253a-254a; Mark Kantor, *International Project Finance and Arbitration with Public Sector Entities: When is Arbitrability a Fiction?*, 24 Fordham Int'l L.J. 1122 (2001) (discussing the *Himpurna* and *Patuha Power* awards).[9]

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[8] Without referencing the substantial size of those awards, Pertamina argues that they establish that the Award in this case is "grossly inequitable – like stepping on the shoulders of a drowning man." Pet. 25. As the district court noted, however, Pertamina's "reliance on *Himpurna* and *Patuha* is also somewhat disingenuous given its argument to the Tribunal that those decisions should not be treated as precedents." Pet. App. 87a, 214a. In fact, Pertamina argued that those awards should not even have been submitted to the tribunal for consideration. Pet. App. 214a.

[9] The *Patuha Power* arbitration was one of the Government of Indonesia's most egregious efforts to thwart an international arbitration. In that case, the Government of Indonesia procured an injunction in Indonesia against further arbitration proceedings, and when the

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The Confirmation Proceedings. Once an international arbitration award has been issued, the New York Convention recognizes two types of actions: (1) an action brought in the country that was the situs of the arbitration (here, Switzerland) to *set aside* the award; and (2) an action brought in any jurisdiction to *confirm and enforce* the award and obtain a judgment. Whereas in the first type of action a party can raise various challenges to the award, in an action to *confirm* the award there are only seven limited circumstances in which confirmation can be denied. *See* 9 U.S.C. § 207; Pet. App. 15a. Moreover, the party opposing confirmation bears the burden of proof of establishing that one of those limited exceptions applies. Pet. App. 15a; *In re Arbitration Between Trans Chem. Ltd. and China Nat'l Mach. Import & Export Corp.*, 978 F. Supp. 266, 309 (S.D. Tex. 1997); *In re Arbitration Between Chromalloy Aeroservices and Arab Repub. of Egypt*, 939 F. Supp. 907, 909 (D.D.C. 1996).

On February 21, 2001, KBC filed suit in the Southern District of Texas to confirm and enforce the Award and to enter a final judgment consistent with it. Pertamina challenged enforcement on just four grounds: (1) the tribunal had improperly consolidated KBC's claims under the ESC and JOC into one arbitration; (2) the arbitrators were not appointed in a manner consistent with the ESC; (3) Pertamina was "unable to present its case" to the tribunal; and (4) enforcement of the damages award would violate the public policy of the United States. Pet. App. 66a-67a.[10]

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arbitration nonetheless continued, forcibly kidnapped and detained the arbitrator it had appointed. 15 Mealey's Int'l Arb. Rep. B-1, B-3 (2000); R. 4294.

[10] Pertamina did not dispute personal jurisdiction in the Southern District of Texas. KBC voluntarily dismissed PLN. Pet. App. 57a, n.1.

Following cross-motions for summary judgment and based on a full record, on December 4, 2001, the district court granted summary judgment to KBC and confirmed the Award, rejecting each of Pertamina's grounds for opposing confirmation.[11] With respect to the sole issue now raised by Pertamina – the propriety of the arbitrators' appointment – the district court first stated that if the arbitral tribunal's decision on that issue were "an arbitrable one," *i.e.*, a decision entitled to deference, there was "no reason under the New York Convention to reject the Tribunal's reasoned analysis of the ESC." Pet. App. 72a.

The district court also considered the appointment issue *de novo*, however, and held that "Pertamina has not established a violation of the ESC in regard to the first (or any other) arbitrator's selection." *Id.* In particular, the district court held that "Pertamina's construction of the selection procedure renders the ESC's arbitration provision illusory" because "Pertamina would hold the unilateral power to prevent the arbitration of disputes between it and KBC arising under the ESC simply by refusing to select or comment on KBC's proposals for an arbitrator." Pet. App. 73a. According to the district court, "[t]hat is not a reasonable interpretation of the expressed intent of the parties as set forth in the ESC." *Id.*

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[11] Prior to the district court's ruling, Pertamina and PLN sought to set aside the Award in Switzerland, the situs of the arbitration. Pertamina and PLN failed to meet the jurisdictional deadline for payment of costs in Switzerland, however, and on April 24, 2001, the Swiss Supreme Court dismissed their appeal for failure to make timely payment. Pet. App. 9a. In August 2001, the Swiss Supreme Court denied their motion for reconsideration. *Id.*

In its *de novo* analysis, the district court agreed with the tribunal's construction of the ESC, but also noted that there are "other viable interpretations of the ESC arbitration clause and the parties' contracts generally that support the procedure used in this dispute." Pet. App. 73a, n.14. As the district court recognized, "because the ESC and JOC are expressly integrated contracts, they must be interpreted together to determine the intent of the parties," and thus the parties may have "intended to be bound by the arbitration provision (including the provision for the selection of arbitrators) *of the JOC when a dispute involved that contract.*" *Id.* (emphasis added). As a result, "the arbitration provision of the ESC would be operative only in the event the arbitration did not include issues arising under the JOC," or the "ESC methodology [might apply] only when KBC and Pertamina both were adverse to PLN and not to each other." *Id.*

As an alternative basis for rejecting Pertamina's arguments on this issue, the district court held that because of the "clear 'pro-enforcement bias' of the New York Convention," Pet. App. 67a (quoting *Compagnie Des Bauxites De Guinee v. Hammermills, Inc.*, No. 90-0169, 1992 WL 122712, *5 (D.D.C. May 29, 1992)), Pertamina had to prove that any violation of the appointment procedures in the ESC had "actually caused Pertamina substantial prejudice in the arbitration." Pet. App. 67a. As the district court held, Pertamina could not make this showing: "there is no evidence – and Pertamina does not even allege – that Prof. Bernardini, the KBC-selected arbitrator, was biased against Pertamina"; "[a]ll the findings and awards were unanimous"; and there "is no evidence or even any allegation that the other two arbitrators were not neutral, were biased, or had any conflict of interest." Pet. App. 74a.

As a final ground for rejecting Pertamina's challenge to the appointment procedures, the district court held that Pertamina's failure to respond to the notice of arbitration or to ICSID's requests for comments on the nomination procedures made the appointment proper:

> The time for Pertamina to object to KBC's selection or for Pertamina to have asserted its right to participate in the first arbitrator's appointment was within thirty days of receiving KBC's Notice of Arbitration and arbitrator selection. *In the absence of an objection from Pertamina, nothing in the ESC precluded the ICSID from accepting KBC's nomination for the first arbitrator. This procedure materially complies with the terms of the ESC.* Pertamina's belated arguments that Prof. Bernardini was improperly selected are a futile attempt to avoid consequences of its strategic decisions not to object timely to KBC's selection and to decline to participate in the selection of an arbitrator.

Pet. App. 73a-74a (emphasis added).

Having failed in its effort to annul the Award in Switzerland (and notwithstanding its prior claims that Switzerland was the situs of the arbitration), following the district court's grant of summary judgment to KBC, Pertamina filed suit in Indonesia seeking annulment of the Award. Pet. App. 10a. An Indonesian court immediately granted an injunction against enforcement of the Award, and in August 2002 annulled the Award. *Id.* In December 2002, Pertamina filed a Fed. R. Civ. P. 60(b) motion in the district court to vacate the summary judgment on three grounds: (1) the Indonesian court's annulment of the Award; (2) newly discovered evidence that KBC's investors held a political risk insurance policy; and

(3) satisfaction of judgment to the extent of a $75 million payment from the insurers. *Id.* Pertamina also filed a motion in the Fifth Circuit to supplement the appellate record and for additional briefing. Pet. App. 92a-93a.

The Fifth Circuit denied Pertamina's motion to supplement the appellate record, and remanded to the district court for consideration of Pertamina's Rule 60(b) motion. *Id.* On remand, the district court denied the motion, holding that the Indonesian Court was not a proper forum in which to set aside the award, Pet. App. 121a; that Pertamina had failed to show that KBC had in any way misled the arbitrators or that KBC's failure to produce the political risk insurance policy violated the rules governing the arbitration, Pet. App. 124a; and that Pertamina was not entitled to set off from the judgment the amount of the insurance payment, Pet. App. 141a. Pertamina appealed that decision, which was consolidated with Pertamina's appeal from the grant of summary judgment to KBC. Pet. App. 3a.

During this period, KBC pursued other confirmation and enforcement proceedings. In March 2003, the High Court of the Hong Kong Special Administrative Region Court of First Instance also confirmed the Award, rejecting the same arguments Pertamina makes here (and the other arguments it made in the courts below) for substantially the same reasons as those articulated by the district court and Fifth Circuit. *See Karaha Bodas Co.*, 335 F.3d at 363; Pet. App. 21a, n.37; 23a; R. 6418; TSR. 6385.[12]

[12] Citations to "R." are to the original Record on appeal in the Fifth Circuit; "TSR." citations are to the Third Supplemental Record on appeal in the Fifth Circuit.

The Fifth Circuit's Decision. The Fifth Circuit affirmed each of the district court's decisions on the issues raised by Pertamina before and after the remand. Pet. App. 3a. Pertamina challenges only one of those holdings here.[13]

With respect to Pertamina's argument regarding the appointment of the arbitrators, the Fifth Circuit did not – as Pertamina contends – defer to the arbitrators (or even to the district court) regarding the propriety of the arbitrators' appointment. Instead, the Fifth Circuit itself interpreted *de novo* the terms of the parties' agreements and rejected Pertamina's arguments:

> If the ESC required KBC and Pertamina jointly to select an arbitrator for disputes in which KBC and Pertamina were opposed, as Pertamina contends, *Pertamina could effectively block arbitration under the ESC simply by refusing to agree*

[13] Although Pertamina does not seek certiorari from the Fifth Circuit's decision on any other issue, Pertamina does state as fact certain contentions that were rejected below. For example, Pertamina states that "only six weeks before the scheduled final hearing, KBC changed its case dramatically," Pet. 12, but the district court found that "[i]n fact, KBC's Rebuttal did not assert any new claims or new legal theories for recovery," Pet. App. 76a, and the Fifth Circuit found that Pertamina's argument was meritless and had been waived. Pet. App. 36a-39a.

Pertamina similarly contends that during the arbitration proceedings, "[u]nbeknownst to Pertamina and PLN, and undisclosed by KBC and its witnesses . . . FPL [a part owner of KBC] was party to a political risk insurance policy." Pet. 12. During the arbitration, however, Pertamina presented evidence from its own witnesses that it was told that KBC initiated arbitration "to claim [for] the insurance company." R. 1031-30, 1390; TSR. 6375. As the Fifth Circuit found, during the arbitration KBC did not produce a copy of the insurance policy owned by some of its investors because of "Pertamina's decisions not to pursue the subject." Pet. App. 50a.

> *with KBC to the selection of an arbitrator. Such an interpretation would make the ESC arbitration clause illusory.*

Pet. App. 32a-33a (emphasis added). Only after concluding that the arbitrators' appointment was consistent with the ESC did the Fifth Circuit note, in a separate paragraph, that the arbitral tribunal had "reasonably interpreted the ESC's arbitration provisions and reasonably applied the UNCITRAL arbitration rules." Pet. App. 33a. At no place in its discussion of this issue did the Fifth Circuit suggest, let alone expressly state, that it was deferring to the arbitral tribunal's decision. The Fifth Circuit *agreed* with the tribunal, but never indicated it was deferring to it.[14]

Like the district court, the Fifth Circuit also found it noteworthy that Pertamina had failed to object to KBC's selection of an arbitrator, to nominate its own arbitrator, or to challenge the arbitrators' appointment until after the entire panel had been selected and seated. The Fifth Circuit held that these actions constituted a "strategic decision that Pertamina should not now be able to assert as a defense to enforcing the Award." Pet. App. 33a.

Pertamina did not petition the panel for rehearing or seek rehearing *en banc*.

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[14] Notably, Pertamina never argued to the Fifth Circuit that it could not defer to the arbitrators' decision on the appointment issue, nor did it cite any of the four appellate decisions that it now argues are in conflict with the Fifth Circuit's decision.

REASONS FOR DENYING THE WRIT

In the opinion below, the Fifth Circuit properly concluded that the arbitrators were appointed in a manner wholly consistent with the arbitration provision of the ESC. That correct interpretation of the parties' contracts and the manner in which the arbitrators were appointed does not present a question warranting this Court's review. Pertamina should not be permitted to avoid its contractual obligations by raising meritless procedural challenges to a properly conducted international arbitration. *Cf. Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 517 (1974) (holding that the "parochial refusal by the courts of one country" to enforce an arbitration agreement or award "would invite unseemly and mutually destructive jockeying" that "would surely damage the fabric of international commerce and trade. . . .").

I. BECAUSE THE FIFTH CIRCUIT DID NOT DEFER TO THE ARBITRATORS REGARDING THE PROPRIETY OF THEIR APPOINTMENT, THE RULING BELOW DOES NOT CONFLICT WITH THE DECISION OF ANY OTHER COURT.

Pertamina's sole argument in support of its petition is that the decision below creates a conflict between the Fifth Circuit and four other courts of appeals on the issue of whether courts may defer to arbitrators when arbitrators have resolved questions regarding the appropriateness of their own appointment. This argument depends entirely on Pertamina's contention that the Fifth Circuit actually deferred to the arbitrators on that issue here. A plain reading of the opinion below, however, demonstrates that the Fifth Circuit did *not* defer to the arbitrators, but

instead conducted its own analysis of the parties' agreements and the facts of this case.

In particular, after recounting the relevant facts regarding the arbitrators' appointment, the Fifth Circuit rejected Pertamina's arguments regarding the arbitration provision of the ESC, holding that if the "ESC required KBC and Pertamina jointly to select an arbitrator for disputes in which KBC and Pertamina were opposed, as Pertamina contends, Pertamina could effectively block arbitration under the ESC simply by refusing to agree with KBC to the selection of an arbitrator." Pet. App. 32a-33a. Such an interpretation, the Fifth Circuit held, "would make the ESC arbitration clause illusory." *Id.* at 33a. Accordingly, the Fifth Circuit concluded, "Pertamina has failed to meet its burden of showing that the Tribunal was improperly constituted." *Id.*

Pertamina nevertheless argues that the Fifth Circuit deferred to the arbitrators when the Fifth Circuit stated that the arbitrators had "reasonably interpreted the ESC's arbitration provisions and reasonably applied the UNCITRAL arbitration rules." Pet. App. 33a. But that single sentence follows the Fifth Circuit's analysis of the facts and the arbitration provisions in the parties' agreements, and thus reflects nothing more than the Fifth Circuit's view that the arbitrators had correctly decided the issue.

Although the Fifth Circuit held that the tribunal had reached the correct conclusion, nowhere did the Fifth Circuit suggest, let alone expressly state, that it was deferring to the arbitrators on this issue.[15] More importantly, nowhere did the

[15] Even Pertamina does not contend that the Fifth Circuit expressly stated it was deferring to the arbitrators decision. *See* Pet. 14

(Continued on following page)

Fifth Circuit even suggest that it would have decided the issue differently than the arbitrators if it had been able to consider the issue *de novo*. *Compare SEC v. Sargent*, 329 F.3d 34, 41 (1st Cir. 2003) ("Although we may disagree with the district court as to which way the equities tip, our hands are tied by the standard of review.").

II. EVEN IF THE FIFTH CIRCUIT HAD DEFERRED TO THE ARBITRATORS, THIS CASE WOULD NOT PRESENT A CIRCUIT CONFLICT WARRANTING THIS COURT'S REVIEW.

A. All Of The Decisions On Which Pertamina Relies Predate This Court's Decision In *Green Tree Financial*.

In attempting to claim that a circuit conflict exists, Pertamina cites to four court of appeals decisions. Each decision, however, predates this Court's recent opinion in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003), which held that courts must defer to arbitrators on matters of arbitration procedures and scope unless those issues are so-called "gateway matters." *Id.* at 452. In the year since *Green Tree Financial* was decided, no court of appeals has interpreted *Green Tree Financial* to decide whether the manner in which arbitrators are appointed constitutes such a "gateway" matter. Thus no court has held that the manner in which arbitrators are appointed is

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(noting that the "court of appeals did not articulate any particular standard of review. . . .").

a "gateway" matter, or that judicial deference to an arbitrator's resolution of that issue is inappropriate.

In *First Options v. Kaplan*, 514 U.S. 938 (1995), this Court held that ordinarily the question of whether the parties had agreed to arbitrate their dispute was an issue that should be decided by a court in the first instance, unless the parties had agreed to submit *that* issue (*i.e.*, the question of whether they had agreed to arbitrate their dispute) to arbitration. *See id.* at 943 ("[A] court must defer to an arbitrator's arbitrability decision when the parties submitted that matter to arbitration."). Eight years later, in *Green Tree Financial*, the question was whether that general rule also applied to conducting an arbitration as a class action. 539 U.S. at 452. Conducting a *de novo* review, the South Carolina Supreme Court had held that the parties' contracts did not permit the arbitral tribunal to conduct a class action. This Court reversed, stating that the issue should have been left to the arbitrators to decide:

> Arbitrators are well situated to answer that question. Given these considerations, along with the arbitration contracts' sweeping language concerning the scope of the questions committed to arbitration, this matter of contract interpretation should be for the arbitrator, not the courts, to decide.

Id. at 453. This Court concluded that "if there is doubt about [who should 'answer the relevant question'] . . . we should resolve that doubt 'in favor of arbitration.'" *Id.* at 452 (citing *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985)).

In reaching this decision, this Court held that there are only "limited circumstances" in which a court should

not defer to an arbitral tribunal's resolution of an issue. *Green Tree Financial*, 539 U.S. at 452. The Court gave two examples of such "gateway" issues: whether there is a valid arbitration agreement between the parties or whether a binding arbitration clause applies to a particular dispute. *Id.* Other issues, including "what *kind of arbitration proceeding* the parties agreed to" and issues "concern[ing] contract interpretation and arbitration procedures," can and should be left to arbitrators to decide. *Id.* (emphasis in original).

By requiring courts to analyze arbitration procedures *de novo* only when they involve "gateway" issues, *Green Tree Financial* suggests that deference should be given to arbitrators when they interpret the parties' agreements in deciding challenges to their appointment, particularly where the parties have committed the resolution of that issue to arbitration. That is precisely what occurred here: the arbitrators interpreted the parties' agreements. Moreover, those agreements incorporated the UNCITRAL Rules, as a result of which "the parties agreed to abide by a system in which the tribunal rules on objections to its jurisdiction and the arbitrator, rather than the district court, should decide whether the parties' disputes are arbitrable." *Wal-Mart Stores, Inc. v. PT Multipolar Corp.*, 1999 U.S. App. LEXIS 31578, *6 (9th Cir. Nov. 30, 1999).[16]

[16] Article 21(1) of the UNCITRAL Rules states that "[t]he arbitral tribunal shall have the power to rule on objections that it has no jurisdiction." (http://www.uncitral.org/en-index.htm). Indeed, because the parties expressly incorporated the UNCITRAL Rules into their agreements, even if the petition properly presented the question of whether the propriety of the arbitrators' appointment was a "gateway" issue, under *First Options* the parties agreed to submit that issue to the arbitrators to decide in the first instance.

Because each case on which Pertamina relies predates *Green Tree Financial*, however, none of those decisions had occasion to consider whether the propriety of an arbitrator's appointment is a "gateway matter" that, under *Green Tree Financial*, must be decided by the courts. KBC is not aware of any court of appeals that has addressed this question in light of *Green Tree Financial*, and this Court should await further development of the law in light of *Green Tree Financial*. *See Brown v. Texas*, 522 U.S. 940, 943 (1997) (denying certiorari because "the likelihood that the issue will be resolved correctly may increase if this Court allows other tribunals 'to serve as laboratories in which the issue receives further study before it is addressed by this Court.'") (citation omitted).

Finally, even if the Fifth Circuit had deferred to the arbitrators on the appointment issue (it did not), only one circuit court had expressly held prior to *Green Tree Financial* that courts cannot defer to arbitrators on the issue of their appointment. *See Cargill Rice, Inc. v. Empresa Nicaraguense Dealimentos Basicos*, 25 F.3d 223 (4th Cir. 1994).[17] In each of the other three cases on which Pertamina relies in claiming that a circuit conflict exists on this issue, the court of appeals simply interpreted the

[17] In *Cargill*, the parties' agreement stipulated that in the event of a dispute, it would be resolved by arbitrators "chosen by mutual agreement," 25 F.3d at 224, and provided that the arbitration could proceed either in Nicaragua or the Rice Millers' Association of the United States ("RMA"), an industry-specific arbitration committee. When the arbitration commenced, the RMA appointed an arbitral committee instead of allowing the parties to do so, as specifically provided by their contract. The Fourth Circuit overturned the award because the parties' contract "expressly required" the arbitrators to be chosen only by the parties. *Id.* Unlike the contracts here, the *Cargill* agreements did not adopt the UNCITRAL Rules.

contracts at issue and did not expressly address whether deference was appropriate. *See Hugs & Kisses, Inc. v. Aguirre*, 220 F.3d 890, 893 (8th Cir. 2000) (no discussion of deference or standard of review in court's reversal of an award against a party that failed to select an arbitrator and refused to participate in the arbitration); *Szuts v. Dean Witter Reynolds, Inc.*, 931 F.2d 830, 831 (11th Cir. 1991) (no discussion of deference or standard of review in court's reversal of an award made by two arbitrators following the disqualification and removal of the third arbitrator where the parties' arbitration agreement expressly provided that no award would be made by less than three arbitrators); *Avis Rent A Car Sys., Inc. v. Garage Employees Union*, 791 F.2d 22, 25 (2d Cir. 1986) (no discussion of deference or standard of review in court's reversal of an award where an arbitrator appointed pursuant to one collective bargaining agreement between the parties determined that a second agreement between the parties applied and proceeded to consider issues under the second agreement).

B. All Of The Decisions On Which Pertamina Relies Involved Domestic Arbitrations To Which The New York Convention Does Not Apply.

There is an additional reason that this case would not present a circuit conflict even if the Fifth Circuit had deferred to the arbitrators on the appointment issue. Unlike the Federal Arbitration Act, the New York Convention – which applies to international arbitrations but not domestic arbitrations – has a specific provision, Article V(1)(d), that addresses whether the confirmation and

enforcement of an international award should be rejected because of the manner in which arbitrators are appointed. *See* 9 U.S.C. § 201, Art. V(1)(d) (recognition and enforcement of an award may be refused only if a party establishes that the "composition of the arbitral authority . . . was not in accordance with the agreement of the parties").

Each of the four cases on which Pertamina relies for its claimed split, however, involved domestic arbitrations, which are not governed by the New York Convention. *See Cargill*, 25 F.3d at 223 (domestic arbitration); *Hugs & Kisses,* 220 F.3d at 890 (same); *Szuts,* 931 F.2d at 830 (same); *Avis Rent A Car Sys.,* 791 F.2d at 22 (same). As a result, none of those cases interpreted Article V(1)(d) to decide whether, in applying it, a court can defer to an international arbitral tribunal's discussion regarding the propriety of the manner in which the arbitrators were appointed – and KBC is not aware of any decision addressing that issue.

Because this is a New York Convention case, prior to this petition, Pertamina had never relied on those four domestic arbitration cases in arguing that in a confirmation proceeding under the New York Convention, a court could not defer to arbitrators on the propriety of their own appointment. In fact, Pertamina never argued to the Fifth Circuit that it could not defer to the arbitrators' decision on the appointment issue, nor did Pertamina cite any of the four court decisions that it now argues are in conflict with the Fifth Circuit decision. Pertamina also never filed an action in any court prior to or during the arbitration to dispute how the arbitrators had been appointed, and instead agreed to have that issue submitted to the arbitrators for their resolution. *See supra* at 9-10.

III. EVEN IF THE DECISION BELOW CONFLICTED WITH A COURT OF APPEALS DECISION AFTER *GREEN TREE FINANCIAL*, THIS WOULD NOT BE AN APPROPRIATE CASE IN WHICH TO RESOLVE THAT CONFLICT.

For the foregoing reasons, the Fifth Circuit's decision does not conflict with the decision of any other court of appeals. But even if there were such a conflict, there are several reasons why this would not be an appropriate case in which to resolve it.

First, the Fifth Circuit's decision on the appointment issue does not rest solely on the court's determination that the arbitrators were appointed in a manner consistent with the ESC. Instead, the Fifth Circuit (like the district court) held in the alternative that Pertamina had waived any right to challenge the propriety of the arbitrators' appointment because Pertamina had failed to object to KBC's selection of an arbitrator, had failed to nominate its own arbitrator, and had failed to challenge the arbitrators' appointment until after the entire panel had been selected and seated. Pet. App. 33a-34a.

Pertamina argues that this alternative holding was "illogical" and incorrect because "no strategic advantage could be gained by failing to take the opportunity to appoint one's own arbitrator if in fact it existed." Pet. 22. But of course that is precisely what *PLN* did: after receiving KBC's notice of arbitration, PLN – which on Pertamina's theory had the right to appoint its own arbitrator – did not object or nominate its own arbitrator. Because nominating an arbitrator is akin to making an appearance, each Arbitration Respondent likely made the strategic decision that if it declined entirely to nominate an arbitrator (or otherwise acknowledge the notice of arbitration), the

arbitration might never get started, or when the arbitration commenced, the Arbitration Respondents could then raise the procedural objection on which Pertamina now relies. In any event, Pertamina does not seriously contend that this fact-specific holding presents an issue that warrants this Court's review, nor does it point to any circuit conflict on this issue.

Second, the district court held as another alternative basis for rejecting Pertamina's challenge to the arbitrators' appointment that Pertamina had failed to prove that any violation of the ESC in the arbitrators' appointment had "actually caused Pertamina substantial prejudice in the arbitration." Pet. App. 67a (citing *Compagnie Des Bauxites*, 1992 WL 122712 at *5). Although the Fifth Circuit did not reach the prejudice issue, the district court's judgment provides yet another ground supporting the decisions below – as does the district court's determination that several alternative interpretations of the parties' agreements supported the manner in which the arbitrators were appointed. *See supra* at 15.

Finally, resolution of the question presented in Pertamina's favor would not affect the outcome of this case or Pertamina's liability to KBC. The petition is based entirely on the argument that the arbitrators' appointment violated the *ESC*; Pertamina has never argued, in this Court or elsewhere, that the appointment of the arbitrators was inconsistent with the *JOC*. The Award, however, held Pertamina liable to KBC for breaching *both contracts*. Pet. App. 232a.[18] As a result, even if Pertamina were to prevail

[18] Although Pertamina argued below that it was improper to consolidate KBC's claims under the JOC and the ESC into a single arbitration, *see* Pet. App. 26a-27a, it no longer presses that argument.

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on its claim that the arbitrators' appointment violated the *ESC*, Pertamina would still be liable to KBC for its breach of the *JOC*. Thus any decision in Pertamina's favor on the appointment issue would be an advisory opinion, exceeding this Court's jurisdiction.[19]

CONCLUSION

For all the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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The arbitrators, the district court, and the Fifth Circuit all rejected this contention, *see* Pet. App. 189a, 69a, 29a, and Pertamina has not presented that issue for review.

[19] This Court "reviews judgments, not statements in opinions," *Black v. Cutter Labs.*, 351 U.S. 292, 297 (1956), and does not ordinarily "decide questions that cannot affect the rights of litigants in the case before" it. *Lewis v. Continental Bank Corp.*, 494 U.S. 472, 477 (1990) (quoting *North Carolina v. Rice*, 404 U.S. 244, 246 (1971)).